

# **STATEMENT OF WOODY ANDERSON CONCERNING AGRICULTURAL TRADE POLICY ON BEHALF OF THE NATIONAL COTTON COUNCIL**

*before the House Committee on Agriculture*

**May 19, 2004**

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## **INTRODUCTION**

Mr. Chairman, thank you for having this hearing today. My name is Woody Anderson. I am a cotton producer from Colorado City, Texas, and currently serve as the Chairman of the National Cotton Council of America.

The National Cotton Council is the central organization of the United States cotton industry. Its members include producers, ginner, oilseed crushers, merchants, cooperatives, warehousemen, and textile manufacturers. While a majority of the industry is concentrated in 17 cotton producing states, stretching from the Carolinas to California, the downstream manufacturers of cotton apparel and home furnishings are located in virtually every state.

The industry and its suppliers, together with the cotton product manufacturers, account for one job of every thirteen in the U.S. Annual cotton production is valued at more than \$5 billion at the farm gate. In addition to the fiber, cottonseed products are used for livestock feed, and cottonseed oil is used for food products ranging from margarine to salad dressing. While cotton's farm gate value is significant, a more meaningful measure of cotton's value to the U.S. economy is its retail value. Taken collectively, the retail business revenue generated by cotton and its products in the U.S. economy is estimated to be in excess of \$120 billion annually. Cotton stands above all other crops in its creation of jobs and its contribution to the U.S. economy.

Any review of the impact of international trade policy on cotton should be undertaken with the understanding that cotton is a raw, industrial product. The economics of cotton production are inextricably linked to textile policy and production, both in the United States and around the world.

The importance of trade to the U.S. cotton industry has never been greater. At some stage of processing, ninety percent of the U.S. cotton crop moves into export channels. In recent years, exports of raw fiber account for more than 60% of total U.S. disappearance. Furthermore, approximately 80% of yarn and fabric produced by our textile industry leaves the U.S. for further processing. It is also the case that many of these exported products are manufactured into consumer goods abroad and return to the U.S. retail market for final consumption. In fact, imported textile products constitute 19 million bales of our 21 million-bale retail market. The success of the U.S. cotton industry is directly impacted by trade policy developments, as well as overall supply and demand conditions in world fiber markets.

This dependence on the export market has been a recent and rapid change for the cotton industry, precipitated by dramatic decreases in U.S. textile production. Cotton producers must now rely on the much more volatile export market as U.S. textile mills only consume about 1/3 of U.S. cotton production.

## **TRADE POLICY DISCUSSION**

### **U.S. / Brazil WTO Dispute Settlement**

It has been a frustrating few weeks for the National Cotton Council and the U.S. cotton industry. We have heard and read the news reports that the Panel hearing the U.S. / Brazil cotton dispute initially ruled against the United States, but we have been unable to read the confidential report. It is, therefore, impossible for me to comment with great precision concerning this apparent ruling.

If the reports I have read are accurate, the Panel ruled against the United States on most of Brazil's substantive points, namely, that the U.S. violated the Peace Clause; that the Step 2 program constituted a prohibited subsidy; that the export credit guarantee program constituted a prohibited subsidy; that the direct

payments we consider to be "green box" do not qualify as green box; and that the domestic cotton program caused "serious prejudice" to the interests of Brazil.

There are different reports as to whether the Panel found a threat of serious injury in the future, so we are completely unsure how to evaluate that component of the decision.

I don't need to tell this Committee how significant this decision may be. We are disappointed, somewhat surprised, and certainly not enjoying the avalanche of editorial writers across the United States using this decision to paint a target on U.S. cotton producers. A bevy of newspaper editorial boards felt obligated to suggest the WTO Panel got it right and the U.S. should just go ahead and offer up the U.S. cotton program to the World Trade Organization, like an old-fashioned sacrificial lamb.

We, of course, strongly disagree. The appeal process will take several more months and even then parties are given a reasonable amount of time in which to conform programs to the WTO ruling. There should be no immediate changes to the U.S. cotton program. It is far too early to begin to speculate what changes will ultimately be considered.

Our industry has been heartened by the statements of support offered by many members of this Committee, the Congress and the Administration. We agree with Ambassador Zoellick that we are in the first stages of a marathon - a race that involves both this dispute settlement action and the ongoing Doha negotiations. We should not and cannot unilaterally disarm under these circumstances.

One article, however, did peak my interest. A Washington Post story on the Panel Report tried to frame the negative decision in the context of the overall agreement. It pointed out that while the decision may appear contrary to U.S. agricultural interests, other parts of the WTO agreement are beneficial to the United States in general and U.S. agriculture in particular.

The cotton industry in the United States has just been dealt a major blow by a decision we believe is incorrect. However, we fundamentally understand the value of the WTO and the agreements that brought it to life. We will fight this decision and its ramifications, but we will also work to ensure that the U.S. cotton program complies with WTO disciplines. A rational, rules-based international trading system is superior to the alternative. We will do our part, working with this Committee and the Administration, to maintain an effective U.S. cotton program that complies with WTO rules.

What concerns us the most is that the U.S. cotton program in 1992 and 1994 was fully coupled to production and had a higher loan rate and target price than any cotton crop subject to the 2002 farm bill. We moved toward decoupling, we slightly reduced loan rates and we reduced the target price, yet today's program somehow was ruled to support cotton at a higher level than we did in 1992. We are perplexed by that result.

We are further concerned with reports that production flexibility payments and direct payments are not considered to be "green box" under the Agricultural Agreement. We do not know the Panel's rationale here, but the U.S. submissions indicate that Brazil essentially argued that no payment program is minimally trade distorting and therefore no payment program is truly green box. This seems clearly contrary to our intent in the Uruguay Round Agreement.

We are troubled that this Panel apparently found a way around clear language in the Uruguay Round Agricultural Agreement exempting agricultural credit guarantee programs from its provisions.

And we are disappointed that a part of the cotton program that was enacted as a part of the loan program back in 1990 and had always been notified to the WTO as an amber box program was determined by this Panel to be a prohibited subsidy and improperly classified.

Most significantly, we are disturbed that parts of this ruling force us to conclude that either the United States does not know what it is agreeing to in the WTO or the WTO agreement is being interpreted contrary to the intent of the contracting members.

In 1993 Sam Hollis, a former President of the National Cotton Council and a cotton warehouseman from Memphis, was in Geneva at the conclusion of the Uruguay Round. Sam was a member of the Agricultural Policy Advisory Committee. As the last parts of the agreement were being concluded Sam asked U.S.

negotiators directly whether Step 2 was to be classified as an export subsidy or as an amber box program. He was told clearly and directly that Step 2 was not an export subsidy but was an amber box program.

In the statement of administrative action accompanying the WTO legislation, Congress was told that the "Export Credit Guarantee Program, one of U.S. agriculture's most effective tools, is among the programs exempt from reduction commitments under the Agreement on Agriculture."<sup>1</sup>

I can't help but speculate what Congress' reaction to the Uruguay Round agreements would have been if it had known that --

- ♦ export credit guarantees were in fact covered by reduction commitments under the Agreement on Agriculture;
- ♦ green box programs are not exempt from actions under the subsidies code; or
- ♦ that cotton's Step 2 program would not be classified as an amber box subsidy.

I am not asserting that any one of our negotiators or the officials establishing policies for those negotiators tried to mislead Congress or U.S. agriculture. There is also nothing partisan in this observation. The Uruguay Round was a bi-partisan negotiation.

I am suggesting, however, that the apparent decision in the Brazil case should raise a caution flag for this Congress, for our current negotiators and for the private sector. It will be very difficult for the U.S. cotton industry to accept at face value interpretations of proposed trade agreements that are not supported by an abundance of clear evidence that will be recognized by the WTO.

It has been the case until now that we have given our negotiators the benefit of the doubt until the final language is completed. Unfortunately, when the final language is completed, we are usually told there can be no changes. If Doha does move forward and we are presented with a new negotiating text, we should make every effort to parse the language and avoid unsupported interpretations. The job of drafting an agreement that should pass muster in the U.S. Congress just got a lot more difficult.

Mr. Chairman, I would be remiss if I did not commend the efforts of the U.S. defense team in this case. They have been led by very capable attorneys from the Office of the U.S. Trade Representative and the Department of Agriculture General Counsel's Office. Joe Glauber in the Office of the Chief Economist at USDA and many other professionals at the Department of Agriculture, in FAS and in ERS, have worked on the U.S. arguments. Their efforts belie the usual portrayal of bureaucrats. These people have cared about this case and their work, and they have gone the extra mile.

## **China**

### **Implementation of WTO**

The Council has raised serious concerns with the way in which the People's Republic of China has implemented its market access commitments under its WTO accession agreement. As a result of our concerns, the U.S. Trade Representative's Office has conducted numerous discussions with China officials in an attempt to get China to modify its implementation of the tariff rate quota (TRQ) for cotton. Our primary objection has been China's allocation of a significant portion of the cotton TRQ to the "processing trade." By allocating quota to the processing trade, China is requiring that apparel made from that cotton be re-exported. Essentially, the processing trade category is not true market access as required by the terms of the U.S. - China WTO accession agreement.

In 2003, China announced revisions to its regulations governing imports of cotton under the TRQ. While those revisions were an improvement and an attempt to simplify procedures, it appears that the processing trade category still exists and that it can still become an impediment to U.S. cotton exports.

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<sup>1</sup> See Volume 1 of the *House Report on the Uruguay Round Trade Agreement*, House Report 103-316, Vol.1, page 734.

However, other events in U.S. - China cotton fiber trade must be noted. China has grown to be the largest importer of U.S. cotton in the world, purchasing over 2.5 million bales in 2003. China announced an additional 2.3 million bales of import quota for 2003 and an extension of the 2003 quota year to June 2004, and has recently announced an additional quota amount for 2004 that reportedly raises the 2004 quota to 8.7 million bales total. The U.S. will undoubtedly provide a large portion of the cotton purchased in China over the next year.

This level of trade with China is beneficial to the U.S. cotton industry and relieves some of the immediacy regarding changes in China's tariff rate quota implementation. China is increasing its cotton tariff rate quotas due to the Chinese textile industry's demands for greater access to the world cotton supply.

Despite this beneficial trade, the United States and the U.S. cotton industry must remain vigilant and continue to push for reform in the TRQ system as required by the WTO agreements. Should internal pressures to purchase foreign cotton subside within China, the private/processing trade distinction that is a part of China's TRQ implementation will once again become a significant barrier to U.S. exports and will exacerbate an ever widening U.S. trade deficit.

### **China – Quality issues**

The Council continues to monitor the manner in which China is instituting a new set of quality standards applicable to cotton fiber sold in China. This new standard would test all cotton for its short fiber content and its nep count to “prevent fake and bad quality cotton from flowing into the market and to fight deceptive practices in the trade.” The U.S. cotton industry has concerns about this new test and believes that there are no cost-effective, reliable tests for short fiber content and nep count.

China has recently announced its plans to totally revamp its cotton handling, inspection and grading systems. There are plans for a specialized government classing agency, the use of HVI classing, maintenance of a central database, permanent bale identification, standard bale sizes, specialized warehouses, a replacement of outdated gin presses, etc. The program is ambitious and calls for it to be phased in over a number of years. It is significant that this program is focused on internal cotton classification and handling and does not appear, at this time, to be targeted to imports.

### **China - textile safeguards**

In late December 2003, the Administration formally requested consultations with China under the special textile safeguard provisions contained in the U.S. - China WTO accession agreement. The request for consultations automatically triggers the quota provisions on three categories of textile products that had been the subject of a safeguard petition filed by the textile industry. The three categories are knit fabric, dressing gowns and brassieres.

The China specific safeguard allows the United States and other WTO Member countries that believe imports of Chinese origin textile and apparel products are, due to market disruption, threatening to impede the orderly development of trade in these products to request consultations with China with a view to easing or avoiding such market disruption. Upon receipt of the request, imports from China may be restricted to a level no greater than 7.5 percent (6 percent for wool product categories) above the amount entered during the first 12 months of the most recent 14 months preceding the request for consultations. The import quotas may last up to one year. China-specific safeguard petitions are filed with the Committee on the Implementation of Textile Agreements (CITA).

The NCC believes the imposition of these import quotas will have virtually no impact on the raw cotton supply/demand situation in China for the 2003/04 marketing year. The average increase in imports from China in knit fabric and nightgowns was more than 800 percent in 2002.

### **Africa**

The U.S. cotton program was the target of a well-orchestrated campaign asserting that the U.S. cotton industry is hurting African nations that depend on cotton as a means to earn export income. Using seriously flawed analysis, several extreme international organizations convinced a few African countries to take on this

cause. The President of Burkina Faso took the unprecedented step of addressing a negotiating group of the WTO to urge it to require the United States to end its cotton program during the summer of 2003.

The attack reached a crescendo when the Chairman of the WTO singled cotton out in the agenda he prepared for the Cancun Ministerial meeting. The cotton sectoral initiative demanded by the four African countries was an immense burden for the process. The publicity generated was excessive. The time that had to be spent by the WTO and by the U.S. delegation in fighting that initiative was excessive.

It was hard to understand why and how cotton was singled out in Cancun. Through its agricultural proposals, the U.S. cotton program had been on the negotiating table from the outset. Instead of joining with the United States to move Doha forward in Cancun, most developing countries used the Africa proposal and other issues to stop progress. The WTO Chairman's unfortunate decision to bring his office into the issue raised hopes among the four African countries. Ultimately, it became clear that these countries were seeking some sort of compensation from the United States or from the WTO and both parties were completely unwilling to do anything that smacked of compensation.

U.S. negotiators took a firm stand against the initiative arguing that any discussion about distortions in world trade in cotton fiber had to be broadened into a sector-wide approach, including man-made fibers and all textiles and had to include discussions on market access for textiles.

As the United States began its attempts this year to re-ignite the Doha Round, the African proposal, while still being discussed, seems to have moved back into the general agricultural negotiations, which is where it belongs.

In the meantime, the National Cotton Council has worked independently and with the Administration to open a dialogue with Benin, Burkina Faso, Mali, and Chad. We have organized informational exchanges with some of these countries. Officials have met with cotton industry executives to better understand the central forces driving investment in cotton and cotton textile production. Efforts are underway to ensure these countries have the opportunity to benefit from biotech-enhanced cottonseed if they so desire. The Council also worked with the Administration to provide a small exemption for African cotton in the rules of origin contained in the Morocco free trade agreement.

These are small steps, but are reflective of our belief that there is more than enough room in the world cotton market for African production and there are meaningful steps these countries can take to reform their systems, increase markets and enhance the returns available to their growers.

The U.S. cotton industry has reacted to the African proposals by looking at the true reasons underlying their complaints, namely, international prices so low that these countries were losing money. We knew that low prices were prevalent for virtually every internationally traded commodity, agricultural and non-agricultural, from 1998 to 2002. This low price phenomena was not associated with any one country's foreign or domestic policies.

We hope we have made progress, and we continue to talk to these countries. I will be traveling to Burkina Faso in June. We intend to host an African delegation to cotton country in July.

We do not intend to offer false hope. We are not seeking to buy off African concerns with fictitious "reforms" of the U.S. cotton program that do not result in true change. We will continue to work with our negotiators in the Doha round in attempting to achieve additional disciplines on agricultural subsidies in a multilateral context.

### **Free Trade Agreements**

The U.S. continues to pursue an ambitious schedule of free trade negotiations. Several are awaiting Congressional consideration at the present time. Reciprocal market access, effective rules-of-origin, no tariff preference levels, strong Customs enforcement provisions and effective rules to protect intellectual property remain the cotton industry's priorities in any free trade agreement.

With respect to cotton fiber imports into the United States, these agreements tend to provide for the immediate elimination of import duties on in-quota cotton fiber, with duties applicable to imports outside the

WTO-negotiated tariff rate quota to be phased out over an extended length of time. From a cotton fiber perspective, these agreements are generally reciprocal and are generally acceptable.

However, the U.S. cotton industry must evaluate each free trade proposal from an agricultural and an industrial raw material perspective. Textile and apparel provisions may have as much or more of an impact on the U.S. cotton industry than do the agricultural provisions.

The North American Free Trade Agreement (NAFTA) remains a true success story for the U.S. cotton industry. It has helped our textile industry compete with low-priced Asian textiles. It is not the answer for long-term U.S. competitiveness in cotton products, but it has been a boost to the U.S. cotton industry from its inception.

The Council has worked for other free trade agreements that would provide benefits to the U.S. textile industry. The key is a rule-of-origin for textile and apparel products that is no less restrictive than those in the North American Free Trade Agreement. A rule-of-origin based on NAFTA-type rules ensures that workers and companies in the United States and the partner country are the beneficiaries of the agreement, not entities in third countries. Anything less opens the U.S. cotton and textile industries to unfair, unbridled competition from countries that will transship textile products in order to take advantage of quota-free, duty-free access to the U.S. NAFTA rules-of-origin provide generally for a yarn-forward rule for cotton textiles and a fiber-forward rule for cotton yarn.

Although the Council has consistently argued against the inclusions of so-called tariff preference levels (TPL's) and other exceptions that undermine the basic rule-of-origin in free trade agreement, most of the agreements have contained some level of TPLs. Some of the more recent awards of exemptions from the applicable rules of origin are excessive.

The Australia agreement contains no TPLs. The Central American Free Trade Agreement (CAFTA) and the Moroccan agreement do contain TPLs.

So far, the United States has agreed to allow third country fabric to qualify as originating goods in an amount equal to 18% of total U.S. apparel production. This is 18% of an industry that seems to decline every year. This 18% free ride is not being granted to fabric made in the countries that negotiated the free trade agreement. It is a free ride being granted to other countries - like China, India and Pakistan - and discourages the development of spinning and weaving capabilities in the participating countries.

When the Administration began negotiating the CAFTA, it stated that there would be no TPLs in this agreement. No free rides for third country fabric. The National Cotton Council and organizations representing the U.S. textile industry supported that stance and worked to achieve a Central American Agreement based on the U.S. position. In the end, that is not the agreement that is going to be signed and presented to Congress for its approval. In place of no exemptions, the agreement includes significant TPLs and "cumulation" for Mexico, undermining the applicable rule of origin.

The National Cotton Council continues to believe that good free trade agreements, particularly in this hemisphere, can help the U.S. textile industry and the U.S. cotton industry. However, the tendency of the United States to agree to provide free trade agreement benefits for textiles from countries that are not part of the deal continues to undermine any potential benefit for the U.S. cotton industry.

A significant economic study performed in conjunction with the National Cotton Council recently concluded that the greatest bearing on the economic future of the U.S. textile industry and, therefore, on the amount of cotton sold to U.S. textile mills, will be (a) the source of textile products imported into the U.S. market, and (b) the source of yarns and fabrics from which the products are made. The only realistic, significant opportunity for improving the economic outlook for the U.S. textile industry is to achieve provisions in trade agreements that foster the use of U.S. yarns and fabrics in textile products that are cut and sewn in this hemisphere. Tariff preference levels achieve the opposite result. They hurt the U.S. textile industry and the U.S. cotton producer.

## **World Trade Organization**

As the United States works to advance the Doha Round of multilateral trade negotiations, the National Cotton Council wishes to reiterate its priorities and comment on several aspects of the draft ministerial text that was developed in Cancun.

### **Improved Market Access**

From the outset of the Doha Round, the National Cotton Council has supported a negotiation that would provide timely, effective and **reciprocal** access to foreign markets for U.S. raw cotton, U.S. manufactured textiles, and U.S. cottonseed and products. We have sought real increases in market access. We are concerned that achievement of these goals is hampered by 1) statements by the United States that it is willing to obtain less than reciprocal market access in non-agricultural products; and 2) an unwillingness of countries with high bound tariff rates to begin reductions from their applied tariff levels.

For many countries, the tariff reductions being discussed would result in no new market access for United States exports. For many countries, the discrepancy between bound tariffs and applied rates under the WTO makes tariff reduction commitments in agriculture virtually meaningless. Real increases in market access for cotton fiber and cotton products should be predicated on tariff reductions from **applied** rates.

### **Tariff Rate Quota Implementation Must Be Improved**

The Office of the U.S. Trade Representative is well aware of the manner in which tariff rate quotas have been implemented in several countries. Often this implementation does not conform with WTO obligations and does not result in the agreed upon levels of market access. While TRQ implementation was a part of initial U.S. Doha proposals, it has faded into the background in recent discussions. The Council urges the U.S. government to ensure that TRQ implementation remains on the Doha agenda and that more clear rules governing the implementation of TRQs be included in any agreement.

### **Developing vs. Developed**

The developed versus developing country dichotomy advanced by some in Cancun was a clear attempt to move the Doha Round negotiations away from reciprocity. While we are sensitive to the needs of many less developed countries, we are not willing to broadly grant liberal, one-way concessions to countries that are as competitive as the United States in world agricultural trade.

Under the current structure of the WTO Brazil claims the same economic position as Mali; China claims the same economic position as Nigeria; and India claims to be in the same stage of economic development as Burkina Faso. We fully support the efforts of Ambassador Zoellick to plug this loophole in the WTO. Truly less developed countries should receive concessions within the WTO agreements. But countries that are competitive in world agricultural trade must stop having it both ways.

### **Trade Distorting Domestic Support**

The United States exhibited a willingness to make substantial reductions in trade distorting domestic support in Cancun and has demanded these reforms since the inception of the Doha Round. The unambiguous position of the United States was largely ignored in Cancun, however, as the U.S. approach requires the rest of the world to make corresponding changes in their trade policy.

Recent draft texts covering the agricultural negotiations have introduced new approaches to disciplines on domestic support that have not yet been fully discussed among United States commodity producers. The draft ministerial text introduced commodity specific limits on amber box support into the negotiation. The U.S. cotton industry needs to achieve a better understanding as to how the United States anticipates such a new discipline would be implemented. We have concerns that product specific amber box limits could detrimentally impact commodity program flexibility from year to year. Such a restriction may cause a difficult adjustment for U.S. agriculture as commodity markets are inherently not stable from year to year.

In addition, recent draft texts also call for a review of green box programs suggesting that these non-trade distorting subsidies may be significantly restricted in a new WTO agreement. As with the prospect of a commodity-specific AMS ceiling, the cotton industry is concerned that unwise changes to the green box classification could also negatively impact U.S. commodity programs and restrict the ability of the United States to carry out effective domestic agricultural policy.

Certainly, the final decision in the Brazil - U.S. cotton case could have a significant impact on the U.S. negotiating position.

### **Singling Out Cotton for Special Treatment**

The U.S. cotton industry believes that a beneficial WTO agricultural agreement will contain substantial market access improvements, an agreement to phase out export subsidies, and significant reductions in, and greater harmonization of, domestic supports by all countries. The U.S. cotton industry is fully prepared to negotiate significant reductions in trade distorting domestic supports as a part of an overall, beneficial agreement. While every product and policy must be on the table for negotiation in the Doha Round, we object to efforts to single out cotton for special treatment. These efforts are unwarranted and undermine a negotiation supposedly dedicated to overall reform.

The United States has correctly observed that trade distortions in cotton are broader than just the production of cotton fiber, encompassing policies regarding manmade fiber and all textiles and apparel. Any meaningful effort at worldwide reform of policies affecting trade in cotton fiber must necessarily include all of these intertwined products. Other countries, however, seem unwilling to truly seek reform in the overall trade in fiber, textiles and apparel, preferring instead to unfairly target U.S. cotton. The strategy of singling out one U.S. commodity for special treatment must be met with a consistent message, namely, that targeting U.S. cotton will not help advance a Doha Round agreement. It will make it more difficult to obtain.

The U.S. cotton industry has not asked for special treatment in this negotiation. It is fully prepared to participate in a meaningful negotiation that contains beneficial concessions by all parties. Feigned complaints that U.S. cotton will escape discipline should the world reach a new agricultural agreement in this round of negotiations should be regarded as what they are - diversionary tactics designed to lead the Doha Round away from a broad-based, reciprocal agreement.

### **Export Subsidies**

The cotton industry supports the U.S. push to eliminate export subsidies in agricultural trade. Export subsidies are no doubt the single most trade distorting mechanism in agricultural trade, causing adverse effects for all non-subsidizing exporting countries, and especially for least developed country exporters. We see no reason for the elimination of export subsidies to be limited to those commodities that are most important to developing countries as we believe different developing countries will have different economic interests. It would be better to eliminate these very distorting subsidies outright.

At the same time, improvements need to be made in WTO rules with respect to downstream subsidization of agricultural products, the use of export taxes to reduce prices of processed products, content requirements for exports and exemptions from taxes for exported products. The refund of special value-added-taxes (VAT) on processed products that are exported is used in many textile exporting countries to subsidize textile and apparel exports. This activity should be classified as an export subsidy, and prohibited.

### **Textiles**

The Trade Act of 2002 set out the principal negotiating objectives of the United States with respect to trade in textiles and apparel articles. It stated that the U.S. is to obtain competitive opportunities for United States exports of textiles and apparel in foreign markets substantially equivalent to the competitive opportunities afforded foreign exports in United States markets and to achieve fairer and more open conditions of trade in textiles and apparel.

The health of U.S. cotton producers has been inextricably tied to the health of the U.S. textile industry since the early 1900's. The U.S. textile industry is not healthy today. Increasing competition from imports has cut

the size of the U.S. textile sector almost in half over the past five years. The apparel sector has shriveled beyond recognition.

The Uruguay Round Agreements provided for worldwide textile quotas to be completely phased out by January 1, 2005. Five years after that agreement was negotiated, China was made a member of the WTO and will be able to take full advantage of the quota phase-out.

It is critical that U.S. negotiators take the textile negotiating objectives seriously in the Doha Round. They must return with an agreement that provides competitive opportunities for U.S. exports of textiles and apparel substantially equivalent to the competitive opportunities afforded textile imports into the United States. In order to achieve this objective --

- foreign tariffs should be made comparable to US tariffs. There should be no further reduction in U.S. textile tariffs until textile tariffs are equalized worldwide;
- non-tariff barriers, which are being increasingly erected to block imports, should be eliminated;
- tariff rate quota implementation should be improved; and
- developing countries that are competitive in international markets with respect to certain commodities or products should be made to conform to trade disciplines that are equivalent to those adhered to by developed countries.

China has stated that because it is a recently acceded member to the WTO it should be given longer time frames in which to implement any future market liberalization under the Doha Round. We disagree. China insisted on being included in textile quota phase-out within the same time frame as countries that were members of the WTO in 1994, essentially upsetting the economic foundation of the Uruguay Round textile agreement. China may face significant transitional issues, but it chose to reap the benefits of WTO membership without delay. It should also shoulder its responsibilities in the same time frame.

#### **Other NCC Objectives in the Doha Round**

The following is a summary list of other objectives the National Cotton Council supports in the Doha Round negotiations:

- Stop the erection of non-tariff trade barriers against agricultural biotechnology products.
- Improve the ability of the WTO to address managed and/or manipulated exchange rates.
- Improve disciplines applicable to the state trading of agricultural commodities.
- Maintain strong U.S. rules to protect against unfair trade practices.
- Do not weaken U.S. countervailing and anti-dumping laws.
- Maintain the ability of the United States to enter into beneficial regional trading arrangements.

The Council supports the new farm bill and believes the policies contained in that bill are consistent with U.S. WTO obligations. Obviously, we disagree with the dispute settlement Panel in this regard.

#### **Export Credit Guarantee Program**

The export credit guarantee program has been an important component of U.S. agricultural policy for well over 20 years. For the past two years the Council has worked with a group of interested trade associations to provide input to USTR and USDA in regard to export credits and export subsidies.

The degree to which the US should accept disciplines on GSM programs depends upon the extent to which the export subsidy programs of the EU and other countries are eliminated, the degree to which monopoly practices of State Trading Enterprises (STEs) are eliminated, and the degree to which real market access is achieved.

Negotiations must start from the commitment in Article 10.2 of the Uruguay Round Agreement on Agriculture to establish disciplines to govern the use of credits which clearly distinguishes between the treatment of credits and export subsidies. Disciplines must cover the full range of credit programs, e.g. export credit insurance, and practices (including those of State Trading Enterprises) for many of which there is a substantial lack of information and transparency that must be addressed. Any negotiated disciplines should be transparent, clearly understood, implemented equitably and with relative ease, and monitored effectively and should prohibit credit programs and similar financial practices that do not comply with WTO rules.

One final point must be made. It is essential that the Doha Round Negotiations continue to be a single undertaking in which the full WTO negotiation is completed prior to implementation of any specific provisions, including disciplines on agricultural export credits.

### **Marketing Access Program**

The Market Access Program and the Foreign Market Development Program continue to be critical components of an effective cotton trade policy. The combined investment of private and public funds, coupled with industry marketing expertise, results in innovative, forward-looking programs that leverage money into high impact campaigns and promotional efforts.

Unfortunately, funding under the FMD program, in particular, has not kept pace in the last two years and needs to be strengthened. We also would encourage the Committee to continue its support for a MAP program funded at its 1992 level of \$200 million.

We must continue to support and fully fund crucial U.S. export programs including the Market Access Program and the Foreign Market Development Program if we are to fairly compete effectively in today's global marketplace.

### **Textile Trade Policy**

The National Cotton Council continues to work with Congress and the Administration to find ways to enhance U.S. textile competitiveness, whether through appropriate changes in costly regulations or through well-designed regional trading arrangements. Despite these efforts, the ability of China to sell textile and apparel products at extremely low prices may shortly swamp the U.S. industry and damage textile industries in other producing countries.

We believe it is important that the textile producing countries of the world evaluate the worldwide impact likely to occur in January 2005 and determine what steps need to be taken in order to ensure the orderly development of world markets in textile and apparel. We have asked the Administration to participate in an international meeting to consider the impact on textile producing countries should the fourth stage of product integration for textiles and apparel occur as scheduled on January 1, 2005. Textile and apparel groups from more than 33 countries around the world, including the United States, have called for this discussion.

### **Biotechnology**

Briefly Mr. Chairman, the Council has been disappointed in restrictions on the products of agricultural biotechnology that have been imposed by several countries around the world. We are convinced that biotechnology is a key component to a more efficient and environmentally conscious agricultural sector. We are actively supporting the efforts of the United States and other agricultural trade associations to ensure that countries do not continue to erect or maintain unfair restrictions on the importation of the products of agricultural biotechnology.

## **ECONOMIC OVERVIEW - COTTON AND INTERNATIONAL TRADE**

### **Outlook for U.S. Raw Cotton Exports**

Since the late 1990's, the U.S. cotton industry has experienced a tremendous shift between domestic mill use and exports. In the 1997/98 marketing year, domestic mill use of 11.3 million bales constituted 60% of total disappearance. Now, just six years later, mill use for the current 2003/04 marketing year is expected to be no higher than 6.3 million bales. Over that same period, exports have increased from 7.5 million bales in 1997/98 to an estimated 13.8 million bales for the current year. If realized, exports would be at an all-time high, surpassing the previous record by almost 2 million bales. Since 2001, exports have constituted more than 60% of total U.S. disappearance.

There are a number of factors behind the dramatic shift in off take of the U.S. cotton crop. Changes in trade policy, China's accession to the WTO, and the strength of the U.S. dollar are just a sample of forces that have accelerated the relocation of cotton spinning from developed to developing countries. To understand the implications for U.S. raw fiber exports, it is important to first evaluate the dynamics in major cotton countries around the world.

### **China**

As the world's largest producer and consumer of raw cotton, it is difficult to overstate China's influence on the world cotton market. Due to their sheer size and the uncertainty surrounding their actions, China tops the list of factors determining world prices and ultimately the price our growers receive.

For 2003/04, USDA estimates that China will spin 31.5 million bales of raw cotton, which is roughly one out of three bales of world consumption. Since 1997/98, China's consumption has grown by 12.4 million bales while all other countries have experienced a net decline of 1.6 million bales. The tremendous growth in their textile industry is fueled by a number of factors. Foreign investment and continued access to credit, even in the cases of non-performing loans, have allowed facility expansion and purchases of new equipment. China also has the advantage of a large supply of low-cost labor. The growth in their cotton mill consumption and textile production has largely occurred due to the expanded access to international markets due to their entry into the WTO in late 2001. China's retail consumption of cotton textile products has been slightly declining in recent years due to intense competition from manmade fibers.

China's growth in mill consumption has not been met with a corresponding increase in cotton production. In 1997 and 1998, China produced approximately 21 million bales and consumed 19 million. By the end of the 1998/99 marketing year, stocks of raw cotton reached an astounding 23 million bales. Since that time, production has fallen short of consumption in each of the last five years, stocks have fallen, and imports have increased. For the current marketing year, poor yields put China's production at 22.4 million bales despite a significant increase in acreage. With production falling 9 million bales below consumption, stocks have declined further and imports are expected to total 8.5 million bales. With 5 million bales of U.S. cotton purchased in this crop year, China has emerged as our largest export customer.

In response to stronger prices, China is expected to increase 2004 cotton acreage in the range of 5-10 percent. Assuming normal yields, production will recover to between 26 and 28 million bales. While this represents a significant increase over last year's level, it will still be well below the expected consumption of 32 to 34 million bales. Assuming no major changes in stock levels, then imports for the 2004/05 marketing year would be in the 5 to 6 million bale range. While lower than the current year, imports are still high by historical standards. Longer term, China is expected to generally be a net importer of raw cotton, although actual levels will be quite variable depending on the size of their own crop.

### **India**

India devotes more land to growing cotton than any other country in the world, but due to low yields, is only the third largest producer behind China and the United States. For 2003, growers in India produced 12.6 million bales, an increase of 2.0 million bales from the previous crop year. In recent years, their production has consistently fallen short of consumption, leaving them as a net importer on the world market. With their

domestic mill use stable between 13.0 and 13.5 million bales, imports range between 1.0 and 2.0 million bales with exports between 40 and 100 thousand bales. The U.S. share of their imports has been quite volatile, ranging from a low of 2% in 1998 to a high of 52% in 2001.

For 2004/05, both production and consumption are expected to increase with little change in the overall trade position relative to the current marketing year. India's position in the world cotton market during the coming years will be dependent on their ability to improve yields through the adoption of biotechnology and more effective water management.

### **Pakistan**

Cotton is the backbone of Pakistan's economy, and the government continues to rely heavily on cotton production as a major source of employment and foreign exchange. With an 8 million bale crop, Pakistan produces the world's fourth largest cotton crop. The government continues to play a large role in Pakistan's cotton industry through various support measures.

Pakistan is also one of the few countries with a growing textile industry. The spinning and weaving industries continue to invest in new equipment as well as to renovate existing equipment. Industry sources generally report that the textile industry is seeking to improve quality as well as to diversify production to include more value-added products, rather than to rely mainly on lower-value yarn exports. As a result, domestic mill use has grown from 7.0 million bales to 9.6 million bales over the past 6 years. The result has been a scenario where imported cotton is needed to supplement domestic production. For 2003/04, USDA estimates that imports will reach 1.9 million bales. Pakistan is currently the largest customer of U.S. pima cotton, and all U.S. cotton constitutes about 40% of their purchases.

The higher prices should induce additional acreage in 2004, and with average yields, Pakistan's cotton crop will approach 9 million bales. However, this will be below expected consumption, which could reach 10 million bales. Strong export demand for textile products is underpinning the increased mill use. Despite the increase consumption, Pakistan's is likely to be a smaller net importer in 2004, with total imports of approximately 1 million bales.

### **Brazil**

Brazil is emerging as a significant cotton producer as acreage expands into the Mato Grosso region. Production for 2003/04 is estimated at 5.4 million bales, a level twice that of just five years earlier. Cotton consumption by Brazil's textile industry remains relatively stable, between 3.6 and 4.2 million bales. In the late 1990's, Brazil imported 1.5 to 2.0 million bales of cotton. The expansion of their domestic production has lowered their imports to less than 500 thousand bales, and subsequently allowed exports to increase. For the current marketing year, USDA estimates that Brazilian exports will reach 1.4 million bales.

Based on current cotton prices relative to soybeans, acreage expansion for the coming year should be fairly modest. If so, then favorable growing conditions will lead to a crop between 5.5 and 6.0 million bales and allow Brazil to maintain its net-exporter position.

In the coming years, available land and favorable growing conditions will allow cotton production to continue to expand. It is also expected that their production will expand at a rate faster than their consumption, allowing much of the additional production to enter export channels.

### **Uzbekistan**

Cotton has traditionally been the primary cash crop in Uzbekistan and an important source of employment and foreign exchange. At the same time, the environmental effects of years of cotton production have caused an environmental and health crisis in the country. Production in 2003 fell to 4.2 million bales, down from 4.6 million the previous year. Although the government's target is 5.5 million bales, actual production continually falls below that level.

Recently, the government initiated a major program to reform the cotton sector, aimed mainly at improving fiber quality. Also, the state determines the area, sets production targets and prices, supplies inputs and

procures and markets the bulk of the crop. With continued support of the government, production in 2004 should climb to approximately 4.5 million bales.

There are also efforts underway to enhance the domestic textile industry, and thus spin more of the crop domestically. For the 2004/05 marketing year, only modest growth is expected in their domestic use, and the bulk of production will enter the export market. Longer term, the stated goal is for the domestic textile industry to consume 50 percent of their cotton production. If realized, this would lead to a decline in raw cotton exports.

### **Turkey**

Turkey consistently produces approximately 4 million bales of cotton. However, within the country, there have been regional shifts as environmental problems reduced area in traditional growing regions and new irrigation infrastructure has allowed expansion in new areas. Stronger prices in 2004 are expected to contribute to additional acres, and production could approach 4.3 million bales. Longer term, production growth will be limited due to competition from high-valued crops.

Turkey's domestic mill use has experienced steady growth in recent years and is estimated at 6.2 million bales for 2003/04. As a result, imports range between 1.8 and 2.8 million bales. Since 2001, Turkey has been a steady buyer of U.S. cotton, with 50-60% of purchases being U.S. growths.

### **Australia**

Australia produces high-quality cotton that competes directly with growths from California's San Joaquin Valley. Prior to a severe drought in 2002, Australia's production averaged 3.4 million bales with 95% moving into the export market. The past two crops have been at 1.7 and 1.4 million bales, respectively, due to a sustained drought.

Recent rains have improved the coming year's production outlook but concerns remain. While production is not expected to reach historical levels, a level of 2.0-2.5 million bales is attainable. This will allow exports to recover but still stay below historical levels.

### **World Totals & U.S. Exports**

Over the past two years, world production has fallen short of consumption by more than 15 million bales, resulting in a significant decline in stock levels. The tighter balance sheet, coupled with China's increased imports, has led to stronger prices since mid-2003. The stronger prices are expected to increase world cotton acreage by 3-7% in 2004, with the degree of increase limited by stronger prices for competing crops. Normal yields would lead to a world crop between 100 and 102 million bales, which would be an all-time high.

Global consumption is not expected to show similar growth and will likely total between 98 and 99 million bales. Continued competition from manmade fibers remains a constraining factor on global demand. Longer term, the greatest challenge facing the world cotton industry is the competition from manmade fibers. With only 5% of world population, the United States, with 20% of global consumption, represents the largest retail market for cotton textile products. For much of the remaining 95% of the population, per-capita consumption of cotton textiles has been flat or declining while purchases of manmade fiber products are on the rise.

With the recovery of global production, ending stocks will rebound by the end of the 2004/05 marketing year.

One of the determinants of U.S. cotton exports is the deficit in the foreign cotton situation, i.e. the amount by which foreign consumption exceeds foreign production. In 2002 and 2003, the deficit was 20.3 and 17.0 million bales, respectively, resulting in significant import demand for U.S. cotton. Obviously, a portion of any shortfall can also be satisfied by reducing stocks, which occurred in both years. Assuming no major weather problems, the gap between consumption and production will fall for the 2004/05 marketing year, and U.S. exports are also likely to decline from this year's high of 13.8 million bales. Our expectation is for exports between 11 and 12 million bales, which would constitute 65% of this year's expected U.S. crop.

## **Outlook for U.S. Textile Trade**

Increasing textile imports over the past several years have devastated the U.S. textile and apparel industries. Despite a retail market that has grown by more than 3 million bales since 1997, U.S. mill use has fallen by 5 million bales over that same period. In 2003, imports of cotton goods topped 19 million-bale equivalents, and further growth is expected in 2004.

Evaluating the textile trade situation and its impact on the U.S. cotton industry is complicated by the two-way trade that occurs with certain countries. The U.S. exports between 4.5 and 5.0 million-bale equivalents of textile products, primarily in the form of yarn, fabric, or piece goods. The majority of these exports go to NAFTA and CBI countries for further processing before coming back to the U.S. in the form of finished goods.

### **U.S. Cotton Product Imports**

With 14.1 million bale equivalents in 2003, apparel is the largest category of imported cotton goods when compared to yarn, thread and fabric, and home furnishings. Imports of cotton home furnishings increased by 20% in 2003 to 2.1 million bale equivalents. Cotton yarn, thread and fabric imports decreased in 2003 to 2.7 million bales, down 9% from the previous year.

Once again, countries in the NAFTA and CBI represented significant sources of imported cotton goods in 2003. Imports from Mexico in 2003 totaled 2.5 million bales, down approximately 4% from the previous year. This marks the third straight year in which imports from Mexico have declined. Imports of cotton goods from Canada also decreased slightly to 564 thousand bales in 2003, down almost 2% from the previous year. Imported cotton goods from CBI for the year are estimated at 3.4 million bale equivalents. This is up more than 10% from the previous year. Combined, the NAFTA and CBI countries accounted for 34% of total U.S. cotton product imports in 2003, down from 36% in 2002. Other top sources of imported cotton goods in 2003 were Pakistan, China, India, Hong Kong, Bangladesh, Vietnam, and Turkey.

For the second consecutive year, the source of imported cotton goods into the U.S. market showing the greatest rate of growth was China. For calendar 2003, cotton product imports from China contain the equivalent of 1.9 million bales of cotton fiber. This is up from 858 thousand bale equivalents in 2001, the final year prior to their WTO accession. It appears likely that China will overtake Mexico in 2004 as the largest supplier of imported product.

For 2004, imports of cotton textile products from all sources are expected to surpass 20 million bale equivalents. Once again, imports are expected to increase at a faster rate than total retail consumption, putting further pressure on the domestic textile industry. However, the greater concerns of the textile industry are reserved for January 1, 2005, when all import quotas are scheduled to be removed.

### **U.S. Cotton Product Exports**

Calendar 2003 marked the second consecutive year of modest growth for exports of U.S. cotton textile and apparel products. Exports grew by 6% in 2003 to 4.8 million bale equivalents. The majority of the increase in exports is due to an increase in cotton yarn, thread, and fabric. Exports of home furnishings increased slightly over the previous year, while exports of apparel declined for the second consecutive year.

The top customers of exported U.S. cotton textiles and apparel in 2003 were once again the NAFTA and CBI countries, with 93% of exports moving into these countries. Exports to the NAFTA countries last year totaled an estimated 1.9 million bales, down 6% from the previous year. Exports to the area accounted for 40% of all U.S. cotton product exports. Exports to the CBI countries totaled 2.6 million bale equivalents or 53% of all U.S. cotton exports in 2003. This is up 18% from 2002 exports of 2.2 million bales, and almost 46% higher than 2000 cotton product exports to CBI.

In 2004, exports of cotton textile products should show modest gains, but still fall below the peak of 5.1 million bales in 2000. Exports to Mexico, our largest customer for textile products, have declined in recent years, but are expected to stabilize in 2004. Growth markets will continue to be countries such as Honduras,

El Salvador, and Colombia. Looking forward, cotton product exports into Western Hemisphere countries are critical to the future of the U.S. textile industry.

### **Conclusion**

The apparent decision by the Panel hearing the Brazil - U.S. cotton dispute serves as a reminder that international trade agreements have real and significant impacts on U.S. industries and on policies carried out by Congress. But we cannot turn back economic forces. The U.S. cotton industry depends on the international market today more than ever before. We know that a rational, rules-based international trading system is superior to the alternative. We will do our part, working with this Committee and the Administration, to construct effective trade agreements and to maintain an effective U.S. cotton program that complies with WTO rules.